

JEFFERIES THINKS INSIDE THE BOX

Team of the month

The UK REITs sector is finding success in becoming more specialised, as Jefferies discovered when it acted as global coordinator and bookrunner for distribution centre owner Tritax Big Box, in a series of equity offerings. Edward Russell-Walling reports.

IN RECENT YEARS, THE REAL ESTATE INVESTMENT TRUST (REIT) MARKET HAS BECOME INCREASINGLY SECTOR-SPECIFIC, with vehicles focusing on a particular type of property. Tritax Big Box REIT specialises in large distribution centres, and recently completed its ninth equity raising in less than four years. Jefferies has been sole global coordinator and bookrunner all along.

For many, REITs' attractiveness comes down to tax. Investors in conventional property firms are effectively taxed twice on company profits, however REITs, which must pay 90% of their property income to shareholders each year, pay no corporation tax. Instead, these dividends are treated as property income to the investor, who is taxed accordingly.

REITs were introduced in the UK a decade ago, joining long-established jurisdictions such as the US and Australia. Since then, most quoted British property companies, including British Land, Hammerson and Land Securities, have converted to REIT status.

GREATER SPECIALISATION

"Like the US, UK REITs are becoming very sector-specific," says Michael Old, Jefferies' European head of real estate investment banking. "The most successful companies in terms of returns have moved to specialise." The range of specialisations is diverse and includes student accommodation, self-storage and doctors' surgeries.



From left: Michael Old, Mark James, Gary Gould

Investors approve. For many of them, it suits their investment strategy to be able to target narrow segments and, in a low-interest-rate environment, they also like the strong dividend yield associated with these vehicles.

Tritax was launched in 1995 as a property management and development firm. It provided investors with exposure to commercial property largely through one-off, standalone funds – one fund for each property – for private clients and family offices. At the same time, it had done a lot of work in logistics, including developing a distribution centre for UK retailer Next that was, at the time, the largest commercial building in the UK.

In 2013, Jefferies was introduced to Tritax by Akur Capital, a small corporate finance adviser that specialises in REITs. "We immediately recognised the attractive qualities of big distribution centres in the UK as an asset class for a new listed REIT," says Mark James,

head of primary distribution in the investment companies team at Jefferies.

The initial public offering (IPO) of Tritax Big Box took place in December 2013, with Jefferies and Akur acting as joint financial advisers, and Jefferies as sponsor, global coordinator and bookrunner. The offer set out to raise £200m (\$256m), and was structured as a 'blind pool'. That meant that management did not reveal its shopping list, for strategic reasons, so as not to tip the market against it. It merely undertook to have all the money invested in appropriate assets within six months.

"It's a good management team and it saw a lot of investors, who all bought into the concept," says Gary Gould, a managing director on Jefferies' UK investment banking team. He and Mr James both worked in Hoare Govett's corporate broking business, acquired by Jefferies in 2012, and now form part of a

specialist investment funds team acting for managers across a range of asset classes.

The £200m was duly raised, at 100p a share. With some leverage (currently about 35% on invested assets), the company acquired six distribution centres for UK retail chain clients including household names such as Marks & Spencer, Sainsbury's, Tesco, Next and Morrisons.

ATTRACTIVE LEASES

"Investors are very comfortable with that level of leverage," says Mr Old. He adds that one of the company's major selling points is a high weighted average unexpired lease term (Wault) – considered desirable, particularly when property markets are soft. "In other sectors, lease lengths are coming down," he says. "But in this sector, planning permission is difficult to get, so availability is scarce and tenants are happy to sign long leases." Tritax Big Box's Wault is 15 years, compared with the five to 10 years typical in other sectors.

Part of the attraction of these distribution centres, or 'big boxes', is that they lie at the heart of the current surge in e-commerce and click-to-buy shopping culture. In the context of sheds, they are very hi-tech. "They typically spend more on fitting them out than the cost of building them," says Mr Old. "So the tenants are very 'sticky'."

Other attractions for investors include the UK focus and high-quality investment portfolio. The company offers geographical and tenant diversification throughout the UK. The quality of the tenants is a plus, as are the upwards-only rent reviews, often with inflation protection. "Because of the undersupply, there is an upwards pressure on rents that you're not seeing in other sectors," says Mr Gould.

A QUICK RETURN

The company did not wait long before returning to the market for more money. It raised a total of £281m in three separate follow-ons in 2014, another £229m in two visits in 2015, and a further £550m in two offerings in 2016. With one exception, in June 2014, each offering was priced higher than its predecessor, rising to 132p in October 2016.

The marketing is an ongoing process – as it needs to be. "I have done four trips with management to the US in the past two years," says Mr James. "We have done non-deal roadshows, seeing institutional investors that can back the company, telling the story, then going back to meet them again."

The exercise is repeated regularly in different parts of Europe. "So if and when the company wants to raise equity, we have

already done a lot of the work, and the investors feel comfortable," he says.

The latest equity offering in May was the first of 2017. Like the others, it was a follow-on rather than a rights issue proper. Some shares were set aside for existing shareholders in an open offer, while others went to new investors via a placing and offer for subscription. An 'intermediaries offer' was made available for wealth management platforms to offer on to their own clients.

"There was a fixed price to all, announced at the launch," says Mr Gould. It was set at 136p per share, midway between the prevailing market price and net asset value (NAV). A feature of Tritax Big Box stock is that it has traded at a premium to NAV ever since the IPO. The offering was priced at a 6.6% discount to the company's pre-announcement closing price, and a 6.7% premium to NAV. That was its largest offer premium yet.

The original idea was to raise £200m, but the offer was significantly oversubscribed, with more than £1bn of demand. So the offering was increased to £350m, of which £213m came from new investors and £137m, via the open offer, from existing shareholders.

BROAD INVESTOR POOL

Aviva has been a shareholder from the start, and BlackRock has been on the register since 2014. But the shareholder base has been evolving over time. "In the IPO, many dedicated REITs investors stayed away because they don't want a blind pool," says Mr James.

So the investor base has been broad from the start, including private banks, family offices and multi-asset investors. "But as the company has grown and as we have continued to engage investors, dedicated REIT investors and other larger institutions have started to come on board," says Mr James. The company's portfolio is now valued at £1.92bn. It says that supply remains highly constrained, and that the UK has the greatest big box need in Europe, requiring 1.7 million square metres of additional space a year to 2020.

Jefferies has raised more than £1.6bn for the company, whose appetite for measured growth shows no sign of waning. Nor does that of investors. Mr Old points out that UK rental yields are very strong and that the market anticipates only limited further tightening.

"But capital growth in real estate can be driven by increasing rentals, and by smart asset management," he says. "Tritax Big Box is a very special case, where the management team, the sector focus, and the demand/supply dynamics of the UK listed sector give it the ability to drive rental value." 



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The Banker
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